COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF THE UNION LIGHT, HEAT AND POWER COMPANY TO ADJUST ELECTRIC RATES	) CASE NO. 91-370

O R D E R

On May 22, 1992, The Union Light, Heat and Power Company ("ULH&P") filed an Application for Rehearing of the Commission's May 5, 1992 Order granting an increase in electric revenues of $22.3 million annually. ULH&P raised 18 issues on rehearing. On June 5, 1992, the Attorney General's Utility and Rate Intervention Division ("AG") filed a response in opposition to ULH&P's application.

CASH WORKING CAPITAL ALLOWANCE

ULH&P claims that the Commission's exclusion of the 10 days of purchased power expense from the determination of its cash working capital allowance unreasonably understates ULH&P's rate base. ULH&P states that the Commission has misinterpreted the Federal Energy Regulatory Commission's ("FERC") modification of the traditional 1/8 formula approach, and that the Commission has failed to apply the formula methodology in a reasonable manner.

As the Commission's May 5, 1992 Order stated, the 1/8 formula approach has traditionally been used in electric utility rate cases. Under this method, the operation and maintenance expenses, exclusive of purchased power expense, are multiplied by 1/8 to determine a cash working capital allowance. Throughout this proceeding, ULH&P has acknowledged that this was the Commission's usual methodology. The only justification offered for the modification for purchased power expense was that ULH&P felt the inclusion of the expense was more reflective of its cash working capital requirements.

As we stated in the May 5, 1992 Order, the FERC modification to the formula approach will allow an adjustment to the results of the 1/8 formula method when it is demonstrated that fossil fuel is a substantial component of the operation and maintenance expenses <u>and</u> the actual lag in payment of fossil fuel is known. If the fuel expense lag adjustment is made, FERC will then allow a further adjustment to the formula results, to recognize the increased importance to the utility of purchased power expense.[1] ULH&P has no fossil fuel expenses nor has it determined an actual lag in payment for either fossil fuel or its purchased power expense. Further, the Commission is not required to adopt the FERC modifications to the formula approach. While ULH&P argues that its position is consistent with the FERC staff top sheets issued in Cincinnati Gas & Electric's ("CG&E") pending wholesale rate case, such top sheets represent only the trial staff's initial positions and are issued for settlement purposes only.

---

[1] May 5, 1992 Order, pages 6 and 7.

The evidence in this case does not persuade the Commission to depart from its past practice to exclude purchased power expense from the calculation of cash working capital utilizing a formula methodology. The Commission has applied the formula methodology in a reasonable and consistent manner. Rehearing is denied.

WEATHER NORMALIZATION

ULH&P contends that the denial of its proposed weather normalization adjustment was unreasonable, resulting in a $1,526,929 overstatement of operating revenues. In response to the Commission's criticisms of the proposed adjustment, ULH&P claims it clearly established that: (1) using degree day data for the latest 30-year period, rather than the 30 years ended 1980, would have very little effect on the adjustment; (2) separating loads into base and temperature-sensitive components would produce the same results as ULH&P's methodology, which included no such separation; and (3) using an earlier test period, as suggested by the AG, would produce results similar to those obtained from ULH&P's adjustment. ULH&P also claims the Commission's concern about ULH&P's methodology is not well founded, as the same method was accepted in its most recent gas rate case.

The Commission finds no merit in ULH&P's arguments. The record shows that ULH&P's attempt to look at the impact of using more current weather data was cursory at most.[2] ULH&P tested the use of base and temperature-sensitive loads on only the commercial

2 T.E., Vol. V, March 23, 1992, pages 224 and 225.

class portion of its adjustment.[3] No attempt was made to verify the temperature sensitive load of the residential class. Minimal and selective analysis, such as that performed by ULH&P, is insufficient to justify an electric weather normalization adjustment.

Irrespective of whether the AG's suggestion to utilize a different test period would produce results similar to those obtained by ULH&P, the methodology has not been shown to be accurate and reliable. ULH&P's comparison to its last gas case is unpersuasive. Residential and commercial gas consumption, which is almost exclusively for space heating, is highly temperature sensitive. In contrast, electric consumption is impacted by numerous factors other than weather, such as economic activity and appliance saturation. ULH&P's adjustment did not consider these other factors and its petition does not attempt to address this issue. Rehearing is denied.

YEAR-END CUSTOMER ADJUSTMENT

ULH&P claims its operating revenues were overstated by $472,516 due to an error in the Commission's calculation of a modified year-end customer adjustment which reflected the impact of denying the proposed weather normalization adjustment. ULH&P states that $287,200, not $756,203, is the appropriate revenue adjustment.

ULH&P's claim is correct. The Commission did err in its calculation of the appropriate revenue adjustment as cited in the

---

3 Id., Vol. II, March 18, 1992, pages 78 and 79.

petition.[4] We similarly erred in calculating the appropriate year-end customer expense adjustment resulting in an overstatement of $379,276. The correct expense adjustment is $245,303, not the $624,579 included in our May 5, 1992 Order. Rehearing is granted for the limited purpose of correcting the calculation of the year-end customer adjustment. Since the correct revenue and expense figures can be calculated from the existing record, no additional evidence need be taken.

FUEL SYNCHRONIZATION

ULH&P contends that the fuel synchronization adjustment adopted by the Commission results in revenues being overstated by $445,574; that it demonstrated the reasonableness of its revised adjustment to reduce revenues by $41,332; that the AG's adjustment, as adopted by the Commission, does not reconcile test year fuel revenues and expenses; and that the adjustment adopted by the Commission does not reflect the impact of the incremental fuel cost resulting from the July 1991 billing adjustment by CG&E. ULH&P states that modifying the adjustment adopted by the Commission to reflect the impact of the July 1991 billing adjustment would produce an adjustment of $207,143 rather than an adjustment of $445,574.

ULH&P's arguments are largely unfounded save for including the impact of reflecting the July 1991 billing adjustment. The

---

4 $472,516 is the difference between the erroneous $756,203 and ULH&P's original adjustment of $283,687. The overstatement, based on correction of the error, is $469,003 ($756,203 - $287,200).

Commission's adjustment did not overstate revenues by $445,574. ULH&P initially proposed an adjustment to reduce revenues by $200,996. The Commission, based on the AG's proposal, increased revenues by $244,578 resulting in adjusted, normalized revenues being $445,574 greater than the level originally proposed by ULH&P. ULH&P did not demonstrate the reasonableness of its methodology in either its original or revised adjustments. As stated in our May 5, 1992 Order and in ULH&P's last rate case,[5] ULH&P's methodology attempts to reconcile revenues for the period ended two months beyond the test period. As this obviously is not the level of revenues included in the test period, such a reconciliation is inappropriate for rate-making purposes.

The Commission did overlook the impact of the July 1991 billing adjustment. Correction of this oversight produces an adjustment of $207,143 as stated in ULH&P's petition, rather than the $244,578 included in our Order. Rehearing is granted to correct this omission and ULH&P's revenue requirement will be adjusted by this Order.

NEWPORT STEEL INTERRUPTIBLE CREDIT

ULH&P contends that it was unreasonable to deny its adjustment to reduce revenues by $1,521,275 to annualize the increased interruptible credit to Newport Steel Corporation ("Newport Steel"). ULH&P argues that since the Commission

5 Case No. 90-041, An Adjustment of Gas and Electric Rates of The Union Light, Heat and Power Company, Order dated October 2, 1990.

previously approved the contract authorizing this credit, rate recovery of the credit cannot now be denied. Referring to our May 5, 1992 Order, ULH&P states it was not aware the Commission's approval of the contract was linked to a presumption that the credit would be recognized at the FERC level by ULH&P's power supplier, CG&E. ULH&P claims that the benefits of interruption and demand reduction have been reflected in CG&E's cost of service and are being shared with ULH&P's customers.

ULH&P's arguments are not persuasive. The Commission's approval of the contract was not linked to a presumption of recognition at the FERC level. The presumption referred to in our rate Order was merely our expression of the implicit and obvious relation between interruptible loads, the credits provided for those loads, and the fact that the generating utility controls the interruptions. As to the benefits of demand reduction being included in CG&E's cost of service, our May 5, 1992 Order and ULH&P's petition are in agreement that CG&E's cost allocation is based on coincident peak demand. Such an allocation does not reflect CG&E's ability to interrupt Newport Steel's load during off-peak, as well as on-peak, hours. The petition offers nothing to change our conclusion that ULH&P's purchased power cost does not equitably reflect the nature of Newport Steel's interruptible load. In addition, the petition does not address the Commission's other reason for rejecting the adjustment, namely ULH&P's failure to recognize increased demand levels for Newport Steel under the new contract. For these reasons rehearing is denied.

AFUDC OFFSET

ULH&P claims that the AFUDC offset adjustment to its net operating income is unreasonable, both in theory and in calculation. ULH&P states that since AFUDC does not represent cash, it is not appropriate to treat the adjustment as test-year revenue. ULH&P notes that the calculation of the offset should have been made using the return on rate base, since AFUDC is included in rate base not capitalization. Finally, ULH&P states that if the offset to net operating income is to be made, a corresponding adjustment to rate base should also be made.

ULH&P originally proposed an adjustment to reflect the increase in the revenue offset which would result from the annualization of AFUDC related to construction work in progress ("CWIP") that is subject to AFUDC. ULH&P acknowledged that in previous rate Orders, the Commission adjusted revenues to reflect AFUDC on test-year-end CWIP, computed at the authorized rate of return. However, ULH&P's proposed adjustment used the AFUDC rate instead of the allowed rate of return, and did not reflect in the adjustment the test-year-end electric balance in Account No. 432, AFUDC - Credit.[6]

In its application for rehearing, ULH&P now argues that any AFUDC offset adjustment is unreasonable. For the first time, ULH&P claims that it does not believe this adjustment is appropriate for the purpose of adjusting test-year revenues, even

---

6 <u>Id.</u>, page 45.

though ULH&P proposed just such an adjustment. The Commission further notes that while ULH&P now claims that a corresponding adjustment to its rate base is necessary, no such adjustment was included in its original proposal. The Commission finds that it is appropriate to use the rate of return on capital for this adjustment. The return on capital represents the overall cost of funds used by the utility to support all elements of the rate base including CWIP.

The Commission determined the AFUDC offset to net operating income in a manner consistent with prior ULH&P rate cases. ULH&P has provided no adequate reasons to rehear this issue.

RATE OF RETURN

ULH&P seeks rehearing on the Commission's authorized return on common equity. The Commission found the cost of common equity for ULH&P to be within a range of 11.0 to 12.0 percent and within this range determined that a return on equity at 11.5 percent would best allow ULH&P to attract capital at a reasonable cost, maintain its financial integrity to ensure continued service and to provide for the necessary expansion to meet future requirements, and also result in the lowest possible cost to ratepayers.[7]

ULH&P asserts that the return authorized by the Commission is so low as to impair its ability to maintain credit and attract

---

7 Case No. 91-370, Application of The Union Light, Heat and Power Company to Adjust Electric Rates, Order dated May 5, 1992.

capital and as a result violates the standards set forth in The Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591, 64 S. Ct. 281, 88 L. Ed. 333 (1944) and Bluefield Waterworks and Improvement Company v. Public Service Commission, West Virginia, 262 U.S. 679 67 L. Ed 1176, P.V.R. 1923 D 11 (1923). ULH&P implies that the Commission has failed to recognize its dual responsibility to the customers and the utility as specifically acknowledged in prior Commission orders. According to ULH&P, "(t)he Commission has historically been aware that a policy which would reduce a utility's credit ratings would drastically increase revenue requirements and hence would increase rates, because of the increased financing costs applied to new capital construction and refinancing indebtedness."[8]

Contrary to ULH&P's assertions, the Commission has not undertaken a policy designed to impair the financial integrity of ULH&P or any other utility under our jurisdiction. The Commission makes an informed judgement based on the evidence presented and current economic conditions. The potential effect of various decisions is inherent in the evaluation of economic conditions for an individual utility. While the Commission's Order in the instant case may not replicate the language of orders issued in 1980, the standards for decision-making are no less relevant. In fact, the Commission's Order of May 5, 1992 explicitly sets forth

---

8 ULH&P Application for Rehearing, May 22, 1992, page 10.

at page 58 the concepts which ULH&P now alleges are the responsibilities which the Commission ignored, that is, "approving the lowest possible rates which are consistent with maintaining adequate service and the financial integrity of the company."[9]

ULH&P compares its authorized return of 11.5 percent to an average return for electrics of 12.4 percent, calculated by Regulatory Research Associates for decisions in the first quarter of 1992, and opines that its authorized return is unreasonable because it is nearly 100 basis points below that average. ULH&P does not mention that the range of returns from which this average was calculated is 11.43 percent to 13.00 percent.[10] ULH&P equates this mathematical average to the return for an average utility and claims that the record "undeniably demonstrates that ULH&P is riskier that the average electric utility."[11] ULH&P did testify that it is riskier than its proxy group of companies;[12] however, none of the 10 utilities from which the mathematical average was calculated were included in ULH&P's proxy of companies of comparable risk or in the AG's proxy of comparable companies. Nor is there any evidence in the record that ULH&P's proxy group represents the average electric utility.

---

9 Id.

10 Regulatory Research Associates, Inc., FOCUS, April 7, 1992.

11 ULH&P Application for Rehearing, May 22, 1992, page 11.

12 Testimony of James M. Mosely, page 22.

ULH&P believes the Commission erred in denying any adjustment for the quarterly compounding of dividends. ULH&P appears to believe that all rate of return witnesses are in agreement with its application of quarterly compounding. The record does not support this belief as is illustrated by evidence presented by the AG.[13] The Commission agrees with the AG that ULH&P's methodology is flawed and that growth in dividends is double-counted. The Commission did not err in concluding that the quarterly dividend model double compensates investors. This decision is not different from previous decisions for ULH&P or any other utility.

ULH&P takes liberties with the Commission's Order by claiming that the Commission "admits" that some flotation cost adjustment should be made. While a flotation cost adjustment may be found reasonable in some instances, a flotation cost adjustment should not be made without adequate support. ULH&P failed to offer this support originally and offered no quantifications in its rehearing petition to address the basis for denial. In short, ULH&P has again failed to meet its burden of proof.

ULH&P testified at length as to the credibility and relevance of its use of credit ratings to establish a proxy group of companies of comparable risk rather than comparable companies for its discounted cash flow analysis. ULH&P admitted the variables of risk differed among its proxy.[14] This was inconsequential

---

[13] T.E., Vol. III, March 19, 1992, pages 26, 31-34.

[14] T.E., Vol. I, March 17, 1992, pages 148-149.

according to ULH&P because credit ratings include an assessment of all kinds of risk. Companies with like credit ratings are viewed by investors as being of comparable risk. The Commission reiterates that if the proxy is truly of comparable risk, no additional adjustment for risk is required.

The Commission finds no basis to grant rehearing on the issue of ULH&P's authorized rate of return.

WAGE ANNUALIZATION

ULH&P claims that the Commission's rejection of its proposed adjustment to reflect the annualization of base wage increases which occurred during the test year is unreasonable, arbitrary, and punitive. ULH&P notes that historically such wage increases have been recognized and allowed in rate proceedings before the Commission. ULH&P states that when wage increases have been disallowed in the past, the decision was based upon a determination that the increase was excessive. Further, ULH&P claims that it was not aware that the allocation of labor hours to which wage increases were applied was a concern of the Commission's until the issuance of the May 5, 1992 Order. Finally, ULH&P states that the Commission is wrong in its assertion that its records are not kept in accordance with the Uniform System of Accounts for Electric and Gas Utilities ("USoA").

The Commission is not limited in determining the reasonableness of a wage annualization to only examining whether the increased wages are excessive. In determining whether a proposed adjustment is reasonable, the Commission must consider whether the adjustment is "known and measurable." If the methodologies used by the utility are not adequate to meet the known and measurable criteria, the adjustment is normally denied. The appropriateness of pro forma adjustments proposed by utilities in each proceeding are evaluated on their individual merits. Consequently, the argument that the Commission has not rejected adjustments of this nature in the past is misleading.

Concerns relating to labor allocation practices were first expressed in the 1989 Management Audit in discussions about the documentation of time studies. In this proceeding, approximately 24 data request items as well as major portions of hearing cross-examination of ULH&P's witnesses addressed this topic. As was noted in the May 5, 1992 Order, the USoA requires that the distribution of employee wages shall be based upon a study of the time actually engaged during a representative period. The Commission found that the current time studies for supervisory, administrative, and professional employees were not based on the actual work performed.[15]

Because the Commission could not determine the reasonableness of the labor hour allocations, it was not possible to verify the reasonableness of the proposed wage annualization. The absence of this verification fully supports our denial of the proposed wage adjustment.

---

[15] Id., page 27.

RATE CASE EXPENSE

ULH&P claims that the rate case expense included for amortization has been unreasonably reduced and the period of amortization is not representative, is arbitrary, and punitive. ULH&P states that its delay in filing the updated rate case expenses was unintentional and had no effect upon the amount of the updated expense. Further, ULH&P states that the total amount of its updated rate case expense is not only reasonable, but was quite low in comparison to other rate proceedings.

ULH&P previously requested relief from the Commission's directive to file monthly updates of rate case expenses during this proceeding. The Commission offered a compromise which required ULH&P to file its last update 20 calendar days after the completion of the public hearing, and ULH&P agreed to this compromise. However, the late filing by ULH&P was not the sole reason for excluding the last updated rate case expenses. As stated in our May 5, 1992 Order, but not addressed in ULH&P's application for rehearing, the costs included in the last update were inadequately documented. Without proper documentation, the Commission can not determine whether rate case expenses are reasonable. ULH&P's rate case expense, like all its other expenses, are not reasonable merely because they are less than those incurred by other utilities. When requested, expenditures must be documented. ULH&P at all times bears the burden of proof in this rate case. Having failed to submit the previously requested documentation, ULH&P has not met its burden.

While ULH&P questioned the period of amortization for the rate case expenses, that period is consistent with prior Commission decisions and strikes a reasonable balance between ULH&P and its ratepayers. The Commission denies rehearing.

POSTAGE EXPENSES

ULH&P claims that the Commission unreasonably denied the proposed annualization of postage expenses. ULH&P states that the Commission's denial of the adjustment, as well as the requirement that postage expenses be directly charged rather than allocated, is inconsistent with past Commission decisions in ULH&P rate cases. ULH&P further states that it is unreasonable and arbitrary for the Commission to disallow these expenses without notice to ULH&P that the standard of reasonableness previously satisfied by it has been changed. Finally, ULH&P claims that no party questioned this adjustment and no evidence challenging the reasonableness of the expenses was introduced.

ULH&P has ignored the fact the Commission denied the proposed adjustment because the postage expense adjustment contained a double count of postage expenses for the first 6 months of the test year.[16] In addition, the Commission has undertaken a more comprehensive review of ULH&P's allocation methodologies due to the ever increasing expense levels. Under normal cost allocation practices, when a cost can be specifically identified the cost should be directly charged to the specific entity, not allocated.

---

[16] Id., page 42.

This would be the case for the expenses for ULH&P's customer bills and its first class letters. No new standard of reasonableness was applied to ULH&P. The finding that ULH&P should be directly charged for postage expense on its customer bills and first class letters resulted from the closer examination of the reasonableness of ULH&P cost allocation practices.

ULH&P has not addressed the Commission's finding that the proposed adjustment would result in a double counting of costs. The claim that the cost allocation practices have been accepted in the past does not constitute grounds for rehearing. Rehearing is denied.

OVERTIME LABOR

ULH&P claims that the Commission unreasonably reduced its test-year overtime labor expense and arbitrarily ordered a modification to its labor allocation procedures which will result in significantly increased costs without any evidence that there will be any benefit from the modification. ULH&P states that the Commission does not understand how it charges straight time and overtime. ULH&P further claims that the ordered change, which has no evidentiary support, will be costly and will provide no benefit to ULH&P or its customers.

We noted in our May 5, 1992 Order that ULH&P has not been able to demonstrate it has taken any actions to control its increasing levels of overtime. The Commission's understanding of ULH&P's overtime labor hour allocations is based on ULH&P's responses in this record. ULH&P has indicated that overtime labor hours are allocated to the same accounts as the regular labor hours, regardless of the source of the overtime hours. Under this practice, it would be possible for overtime hours generated in ULH&P's electric operations to be allocated to its gas operations, and vice versa. The Commission finds that this is not an appropriate allocation methodology. ULH&P has performed no analysis to support this assumption in its allocation practices. Also, there is no evidence to demonstrate that ULH&P's current practice results in a reasonable allocation. ULH&P has the burden of proof in demonstrating its labor allocation practices are reasonable. In this instance, ULH&P has not met its burden. Rehearing is denied.

METER READING WORKFORCE REDUCTION

ULH&P claims that the Commission unreasonably removed $125,000 in test-year salaries associated with the re-routing of its meter reading routes, a project recommended in the 1989 Management Audit. ULH&P states that the re-routing permitted a reduction of 4 employees, which occurred after test-year end. ULH&P further states that the Commission may not assume that the wage reduction may be used to reduce test-year electric expense. Finally, ULH&P notes that the $125,000 was for ULH&P in total, not just electric operations.

The Commission notes that while the actual reduction in employees occurred after test-year end, this management audit recommendation was ongoing throughout the test year. Consequently, some associated expenses were included in the test-year expenses. While it is not specifically identified in the record, the reduction in employees occurred between test-year end and January 1, 1992. ULH&P was able to estimate the $125,000 reduction in its September 1, 1991 Management Audit Status Report. ULH&P has not explained why the wage reduction is not an appropriate known and measurable change which would reduce test-year electric expense.

Prior to the filing of ULH&P's application for rehearing, the record in this proceeding was not clear as to whether the $125,000 reduction applied to electric operations only or to total company. Accepting as we will ULH&P's representations that the $125,000 covered both gas and electric operations, it would not be appropriate to deduct the gas portion from electric operations. Further, the Commission finds that the adjustment to operating expenses should be computed using the electric allocation factor used in determining the overtime labor adjustment, as shown in Appendix C of the May 5, 1992 Order. Allocating 71.45 percent[17] of the $125,000 to electric operations results in an increase in ULH&P's pro forma operating expenses of $35,687.

INCOME TAX EFFECTS

ULH&P requested that the tax effect of any adjustments resulting from rehearing issues be flowed through to the test year results for purposes of adjusting its rates. The Commission agrees and the income tax impact of the adjustments described herein has been recognized in the determination of revised revenue requirements.

---

[17] Id., Appendix C.

RESIDENTIAL RATE DESIGN

ULH&P argues that the decision to impose an inverted block summer rate is not supported by the evidence of record and is punitive for customers with all electric service. ULH&P contends such a rate design indicates that all consumption over 1,000 KWH during the summer months is an inefficient use of electricity and insinuates that users over 1,000 KWH per month are the sole contributors to ULH&P's summer peaking characteristics. ULH&P also argues that the rate design and revenue distribution violates the rate design principles of gradualism and continuity.

The AG presented substantial evidence supportive of an inverted block summer rate[18] and ULH&P's rebuttal testimony included data supportive of such a rate design.[19] The inverted rate design approved by the Commission is not punitive nor does it insinuate that consumption over 1,000 KWH is either an inefficient use of electricity or the sole contributor to ULH&P's summer peaking characteristics. The inverted block rate merely gives recognition to ULH&P's summer peaking characteristics and attempts to send a price signal that will reduce demand, and costs, during the peak summer season.

---

18 Kinloch Direct Testimony, pages 42 through 52, and Exhibits DHK-7 through DHK-17.

19 Ochsner Rebuttal Testimony, page 4, and Schedule PFO-R2.

ULH&P's claim that the rate design violates the principles of gradualism and continuity is unfounded. Overall revenues were increased by 15.0 percent, and that same increase was applied to the residential class. A small customer using 500 KWH in the summer received an increase of 13.6 percent while a large customer using 2,000 KWH received a 17.5 percent increase. Given that these variances from the overall percentage increase (.91 and 1.17, respectively) are comparable to the 1.2 factor ULH&P employed to achieve gradualism in its proposed residential increase, the Commission finds no basis for ULH&P's claim. Rehearing is denied.

LATE PAYMENT PROVISION

ULH&P claims the modification to its late payment provision as ordered by the Commission will result in customer confusion and dissatisfaction, and unnecessary expense to itself. ULH&P contends these problems will arise because this is an electric case and the modification will not apply to gas service; therefore, electric customers will be treated one way, gas customers another, and combination customers still another regarding late payment matters. ULH&P claims our decision creates a disincentive for a customer to pay his or her bill timely and will cause customers who make timely payments to subsidize late payments. ULH&P also claims that customers subject to disconnection for non-payment would be harmed because the amount of payment applied to the customer's past due balance would not be enough to allow ULH&P to cancel the non-payment disconnection order.

The Commission did not change ULH&P's late payment provision. We merely directed ULH&P to change the manner in which it credits payments received from customers with outstanding past due balances. As this is a procedural change, as opposed to a rate change, the Commission considers this a common area applicable to both electric and gas service. The change is to be applied consistently to all customers be they electric, gas, or combination customers. Our rate Order failed to express this intent.

If customers do not make timely payments, the late payment charge is to be applied in the manner it has been applied in the past. It is when a customer with an outstanding past due balance makes a timely payment sufficient to cover the current month's bill plus at least $5 toward the past due balance that the change in procedure occurs thereby eliminating a late payment charge on the following month's bill. The argument that customers subject to disconnection might be harmed is specious. Payment received from such a customer, regardless of how credited, should be recognized in ULH&P's system as sufficient action to cancel the pending disconnection order. This procedural change was previously mandated for the Louisville Gas and Electric Company in its most recent rate case[20] and no reason has been presented to

---

20 Case No. 90-158, Adjustment of Gas and Electric Rates of Louisville Gas and Electric Company, Order dated December 23, 1990.

convince us that this change will not be highly beneficial to ratepayers with no additional burden on ULH&P. ULH&P has advanced no issues not previously considered in our decision making. For these reasons, rehearing is denied.

COST OF SERVICE

ULH&P requests reconsideration of the Commission's requirement that distribution plant be separated into primary and secondary components for use in ULH&P's next cost-of-service study. Reiterating that its accounting records are not maintained in a manner that separates primary and secondary plant, ULH&P contends that complying with such a requirement will be costly and time consuming. ULH&P requests that it be permitted to study the matter and, if feasible, present an allocation methodology in its next electric rate case for separating primary and secondary plant. If it is unable to develop a methodology, ULH&P proposes to provide testimony explaining the reasons for its inability.

The Commission is persuaded to modify its Order to allow ULH&P to respond in the manner suggested in its petition. The Commission expects ULH&P to follow the intent of our May 5, 1992 Order, however, and use the methodology it develops to allocate primary and secondary plant in its next cost-of-service study, or be at risk of having its study rejected.

MANAGEMENT AUDIT ISSUES

ULH&P notes the Commission's expressed exception with ULH&P's allocation of administrative and general expenses. ULH&P indicates that these concerns were related to an issue raised in the 1989 Management Audit. ULH&P states that it had provided substantial data to, as well as met with, the Commission's Management Audit Branch on this issue and believed that the issue had been placed in the "completed" status. ULH&P perceives that the Commission and its Management Audit Branch are not in agreement concerning these allocation practices. ULH&P requests that the Commission instruct its Staff and ULH&P to work together to resolve any differences and present the Commission with a resolution of this issue.

In a letter to ULH&P dated November 13, 1991, the Management Audit Branch stated that the placement of recommendations III-10 and III-11 in a "completed" status should not be viewed as either an acceptance or approval of ULH&P's cost allocation process or methodology. In addition, the Management Audit Branch stated that cost allocations arising from affiliated relationships are regularly addressed during rate proceedings and ULH&P should be prepared to fully address any questions on such issues in that context.

The Commission finds no basis for ULH&P's requested modification to the May 5, 1992 Order. Therefore, the request to modify is denied.

PRACTICES AND PROCEDURES

ULH&P notes that in the May 5, 1992 Order the Commission took issue with ULH&P's allocation of administrative and general expenses, allocation of overtime hours, allocation of work hours based on the seasonal neutral month of May, legal department time recording, and the determination of the impact of increased FICA taxes. ULH&P states that it has been directed to take action to modify these practices and procedures, which have been consistently used by ULH&P and accepted by various commissions, including this Commission. ULH&P claims that since no other practical procedures have been offered in evidence or known to exist, these directives are clearly unreasonable. ULH&P suggests that these practices and procedures should be reviewed in an investigation outside of a rate proceeding before it is arbitrarily ordered to make modifications. ULH&P requests that the Commission modify the May 5, 1992 Order regarding these practices and procedures.

Concerns about these various practices and procedures have been raised before in either the 1989 Management Audit or during Case No. 90-041.[21] Contrary to ULH&P's belief, it is not being penalized for the continued use of these practices and procedures. However, as has been stated earlier, ULH&P's allocation practices and procedures were reviewed more closely in this proceeding than they were in the past. ULH&P's application for rehearing ignores the Commission's May 5, 1992 findings concerning these practices and procedures:

1. The allocation of administrative and general expenses relies on time studies which are not based on actual time worked.

2. The allocation of overtime hours does not reflect the source of those hours.

---

21 Order dated October 2, 1990.

3. ULH&P has not verified its determination that the month of May is a seasonal neutral month.

4. The legal department time recording methodology needs to be reconsidered.

5. The adjustment to FICA taxes should reflect the same time period as that used for wage adjustments.

ULH&P has the burden of proof to demonstrate that these practices and procedures result in reasonable allocations of expenses to be included in customer rates. In this proceeding, ULH&P failed to meet this burden of proof. ULH&P has offered no compelling reasons to modify the May 5, 1992 Order regarding these practices and procedures. The request to modify is denied.

REVENUE REQUIREMENTS

Based on the Commission's decision, the Commission has recalculated the additional revenue required by ULH&P. The revised operating income and the increase in revenue allowed is as follows:

Net Operating Income Found Reasonable	$ 8,997,310
Adjusted Net Operating Income	(4,474,107)
Net Operating Income Deficiency	13,471,417
Gross Up Revenue Factor for Taxes, PSC Assessment, and Uncollectibles	1.66979
Additional Revenue Required	22,494,380

The additional revenue granted will provide a rate of return on the net original cost rate base of 9.80 percent and an overall return on total capitalization of 10.11 percent. The rates and charges in Appendix A are designed to produce gross operating revenues, based on the adjusted test year and the adjustments described herein, of $170,811,963.

IT IS THEREFORE ORDERED that:

1. Rehearing be and it hereby is granted on the issue of the appropriate year-end customer adjustment for the purpose of correcting the adjustment.

2. Rehearing be and it hereby is granted on the issue of the appropriate fuel synchronization adjustment for the purpose of correcting the adjustment.

3. Rehearing be and it hereby is granted on the issue of the appropriate electric adjustment for meter reading workforce reduction for the purpose of allocating the total adjustment between gas and electric operations.

4. The additional revenue increase resulting from the adjustments addressed in the preceding paragraphs is $159,438; and ULH&P should be entitled to prospective recovery of this increase.

5. Rehearing be and it hereby is granted on the issue of cost of service to the extent that ULH&P shall be permitted to present its next cost-of-service study based on its allocation of distribution plant into primary and secondary components.

6. Rehearing on all other issues be and it hereby is denied.

7. The rates in Appendix A be and they hereby are approved for service rendered by ULH&P on and after the date of this Order.

8. All other provisions of the Commission's Order of May 5, 1992 shall remain in full force and effect.

Done at Frankfort, Kentucky, this 11th day of June, 1992.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Executive Director, Acting

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 91-370 DATED June 11, 1992.

The following rates and charges are prescribed for the customers in the area served by The Union Light, Heat and Power Company. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

ELECTRIC SERVICE RATES

RATE RS
RESIDENTIAL SERVICE

Energy Charge	
Summer Rate	
First 1,000 Kilowatt-Hours	6.812¢ Per KWH
Additional Kilowatt-Hours	7.274¢ Per KWH
Winter Rate	
First 1,000 Kilowatt-Hours	6.812¢ Per KWH
Additional Kilowatt-Hours	5.366¢ Per KWH

RATE DS
SERVICE AT SECONDARY DISTRIBUTION VOLTAGE

NET MONTHLY BILL

Computed in accordance with the following charges provided, however, that the maximum monthly rate, excluding the customer charge and the electric fuel component charges, shall not exceed 19.869 cents per kilowatt-hour.

Demand Charge:	
First 15 Kilowatts	$0.00 Per KW
Additional Kilowatts	$6.85 Per KW

Energy Charge	
First 6,000 KWH	7.197¢ Per KWH
Next 300 KWH/KW	4.389¢ Per KWH
Additional KWH	3.634¢ Per KWH

For customers receiving service under the provisions of former Rate C, Optional Rate for Churches, as of June 25, 1981, the maximum monthly rate per kilowatt-hour shall not exceed 11.785 cents per kilowatt-hour plus the applicable fuel adjustment charge.

RATE DT
TIME-OF-DAY RATE FOR SERVICE AT DISTRIBUTION VOLTAGE

Demand Charge	
Summer	
On Peak KW	$10.21 Per KW
Winter	
On Peak KW	$8.43 Per KW
Energy Charge	
All KWH	3.659¢ Per KWH

RATE EH
OPTIONAL RATE FOR ELECTRIC SPACE HEATING

Energy Charge	
All KWH	5.376¢ Per KWH

RATE SP
SEASONAL SPORTS SERVICE

Energy Charge	9.002¢ Per KWH

RATE GS-FL
OPTIONAL UNMETERED GENERAL SERVICE RATE FOR SMALL FIXED LOADS

For Loads Based on a Range of 540 to 720 Hours Use Per Month of the Rated Capacity of the Connected Equipment	7.086¢ Per KWH

For Loads of Less Than 540 Hours Use Per Month of the Rated Capacity of the Connected Equipment	8.168¢ Per KWH

RATE DP
SERVICE AT PRIMARY DISTRIBUTION VOLTAGE

Demand Charge:	
All Kilowatts	$6.36 Per KW
Energy Charge	
First 300 KWH/KW	4.438¢ Per KWH
Additional KWH	3.653¢ Per KWH

RATE TT
TIME-OF-DAY RATE FOR SERVICE AT TRANSMISSION VOLTAGE

Demand Charge	
Summer	
On Peak KW	$6.93 Per KW
Winter	
On Peak KW	$5.66 Per KW
Energy Charge	
All KWH	3.609¢ Per KWH